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In the Supreme Court of the United States

OCTOBER TERM, 1946

IN THE MATTER OF PITTSBURGH RAILWAYS COMPANY, DEBTOR

No. 359

PHILADELPHIA COMPANY, PETITIONER

v.

JULES GUGGENHEIM ET AL.

No. 360

PHILADELPHIA COMPANY, PETITIONER

v.

CITY OF PITTSBURGH

No. 361

PHILADELPHIA COMPANY, PETITIONER

v.

HORACE F. BAKER AND JOHN A. BEATTIE, PROTECTIVE COMMITTEE, ETC.

No. 362

MONONGAHELA STREET RAILWAY COMPANY AND PITTSBURGH AND BIRMINGHAM TRACTION COMPANY, PETITIONERS

v.

JULES GUGGENHEIM, ET AL.

No. 363

MONONGAHELA STREET RAILWAY COMPANY AND PITTSBURGH AND BIRMINGHAM TRACTION COMPANY, PETITIONERS

v.

CITY OF PITTSBURGH

No. 364

MONONGAHELA STREET RAILWAY COMPANY AND PITTSBURGH AND BIRMINGHAM TRACTION COMPANY, PETITIONERS

v.

HORACE F. BAKER AND JOHN A. BEATTIE, PROTECTIVE COMMITTEE, ETC.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

PRELIMINARY STATEMENT

The Securities and Exchange Commission, pursuant to Section 208 of the Bankruptcy Act (Act of June 22, 1938, c. 575, § 1, 52 Stat. 894, 11 U. S. C. § 608), became a party to the proceedings for the reorganization of Pittsburgh Railways Company, debtor, under Chapter X of the Bankruptcy Act in the District Court for the Western District of Pennsylvania. The district court, adopting a Special Master's findings of fact with immaterial modifications, and also his conclusions of law, held that it lacked jurisdiction to comprehend in the debtor's reorganization numerous so-called underlier corporations comprising integral parts of the debtor's street railway system. The Commission had taken a contrary view before the district court and was a party to the appeals from its order. The circuit court reversed, holding that the necessary jurisdiction existed.

OPINIONS BELOW

The opinion of the circuit court of appeals (R. 939–952) is reported at 155 F. (2d) 477. The opinion of the district court (R. 133a–151a) is reported at 60 F. Supp. 600.

JURISDICTION

The judgments of the circuit court of appeals were entered May 7, 1946 (R. 952–954). A petition for clarification of opinion was denied June

28, 1946 (R. 955–964, 970). Petitions for writs of certiorari were filed August 5, 1946. Jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, c. 229, § 1, 43 Stat. 938, 28 U. S. C. § 347.

QUESTION PRESENTED

Whether a reorganization court for the debtor, which operates an inextricably integrated urban traction system comprising its properties and those of forty-nine "underlier" corporations, can assert jurisdiction over such corporations and their properties for the purpose of entertaining a plan of reorganization comprehending the entire system, where the properties in question are in the custody of the court, where the functional unity of the system as well as the public interest prevents its dismemberment, where the underliers' right to repossession under their leases and operating agreements is therefore purely theoretical, where the bulk of the underliers are insolvent, and where no feasible alternative appears to a system-wide reorganization.

STATEMENT

In the view of the Commission, the determination of the question of jurisdiction depends wholly upon the unusual factual situation the case presents. It is impracticable to present here all the details and complexities confronting the courts

below; accordingly we confine our statement to the facts that are important to an understanding of the Commission's position. Basic to its views is the finding that the assets comprising the debtor's street railway system have for nearly half a century been operated as an inseparable economic and physical unit (R. 951).

Formation of the system—The underliers

The present system came into being in 1902, when several transit groups operating in Pittsburgh were amalgamated by Philadelphia Company, petitioner in Nos. 359–361, into one unified system operated by the debtor, which it controlled (R. 639, ¶¶ 91–92[1]). This was the culmination of a process of integration which, assertedly pursuant to Pennsylvania statutes authorizing street railway unification,[2] had been under way previously and in which Philadelphia Company participated (R. 632–638, ¶¶ 61–82). The 1902 unification took the form of (1) long-term leases from several underliers to Consolidated Traction Company and United Traction Company of Pittsburgh (both being underliers whose stocks were controlled by Philadelphia Company and both already lessees of numerous other underliers) (R.

[1] Paragraph references are to the Special Master's Report (R. 604–837) on the petition of the City of Pittsburgh (R. 40a–83a) to assert jurisdiction over the underliers. A summary of the facts found by the Special Master appears in his report at R. 806–814, ¶¶ 1001–1026.

[2] See statutes cited at R. 948, n. 11, 12; R. 826–828, ¶ 1072.

634–635, ¶ 68; R. 637–639, ¶¶ 75–78, 92) and (2) so-called short-term operating agreements authorizing the debtor to operate the properties owned by or leased to United and Consolidated.

The system at present contains 49 underliers over which jurisdiction was asserted.[3] Of these, 36 are controlled by the debtor by 100% or majority stock ownership, or are its affiliates through similar stock ownership by Philadelphia Company, the debtor's parent (R. 806, ¶ 1001). These 36 are referred to as "Philadelphia Underliers." The stocks of the thirteen other underliers, while largely held by the public (*id.*), are in part owned by Philadelphia Company (R. 618, ¶ 26), and these underliers are in addition linked to the debtor by physical and contractual ties. Of the 13, nine (4 companies, one having stock control over 5 others, R. 794–803, ¶¶ 831–876; R. 538a–539a) are the so-called "Guaranteed Underliers,"[4] whose leases were guaranteed by Philadelphia Company.

These guarantees resulted from a contract, entered into as part of the 1902 unification, between Philadelphia Company and A. W. Mellon, then in control of Pittsburgh & Birmingham Trac-

[3] The underliers are listed at R. 77a–80a, and tables and charts of their intercorporate relations appear at R. 81a, 82a, 538a, 539a, 584, 650–651, and 846. In addition to the 49 underliers there are 3 others over which jurisdiction was not sought (R. 547).

[4] One other Guaranteed Underlier, Mount Oliver Incline Railway Co., is not included in the total of nine. It is one of the three underliers over which jurisdiction was not sought.

tion Company and Monongahela Street Railway Company. Pursuant to the contract, the two Mellon companies executed 900-year leases of their properties[5] to United and Consolidated, respectively, while a third company, Suburban Rapid Transit Railway, executed a similar lease of its properties to Consolidated (R. 639–643, ¶¶ 91–122). These leases imposed upon United and Consolidated the obligation, *inter alia,* to pay as rentals to the lessor companies sums "available for dividends" on their stocks, to pay the lessor companies' taxes, to meet their interest payments and to "unite" in meeting their maturities (R. 889–892, 906, 908, 926, 928). These lease obligations were undertaken by the debtor pursuant to its contemporaneous operating agreements with United and Consolidated (R. 654, 655, ¶¶ 164, 166). Performance by the lessees under the three leases was guaranteed by Philadelphia Company (R. 900, 909, 936). The principal companies among the nine Guaranteed Underliers are the petitioners in Nos. 362–364.

The four remaining companies, whose stock is publicly held and whose contractual ties with the debtor lack Philadelphia Company's guarantee (R. 804–806, ¶¶ 891–901), are called "Unguaranteed Underliers."

[5] The properties of Pittsburgh & Birmingham comprised leasehold interests conveyed by its five stock-owned companies and one other lessor company (R. 798, ¶ 851, R. 902–905).

The foregoing three groups of underliers, together with the debtor and some other companies not here involved, comprise the present system.

Unitary character of the system

The properties of the debtor and the underliers are operated by the debtor through a complicated series of direct and indirect leases, assignments and operating agreements (R. 648–653, ¶ 158). Since the 1902 amalgamation, operations have been conducted on a unified basis, and with a commingling of the properties of the debtor and the individual underliers and a disregard of the corporate entities of most if not all of them.

The system is centrally administered (R. 667-669, ¶¶ 214–219). Routes, schedules, fares, transportation, maintenance and renewals, and accounting for revenues and expenses are performed on a system-wide basis, with no concern for the underliers (R. 669–675, ¶¶ 221–255; R. 540a). As the court below observed (R. 945–946):

> * * * the system operates as a unit. This is more clearly demonstrated when a few particulars are given. For instance, one trolley route covers thirty different franchise segments belonging to ten underliers. Other routes use the franchises of thirteen different underliers. Operating employees know nothing about the separate

underlying companies and neither does the travelling public. All receipts are put in a common pot.

Underliers' assets have been commingled and disposed of in accordance with system needs. Under the debtor's control of the system, numerous stretches of underliers' franchised track were abandoned (R. 730–733, ¶ 515), and reconstitution of the lines of the pre-1902 operating companies is either impossible (R. 795, 799, ¶¶ 834, 852) or would require extremely impracticable rearrangement of trackage rights (e. g., R. 758–770, ¶¶ 671–702). In 1902 the underliers owned nearly 1,300 cars; only 32 of these remain, none in passenger service (R. 729–730, ¶ 514), and title to the 1,000 passenger cars now in use has been taken in the name of the debtor, whose property they are presumed to be (R. 754, 739, ¶¶ 633, 541). Power properties and carhouses belonging to underliers in 1902 have been dismantled, razed or sold (R. 727–729, ¶¶ 512, 513; R. 733–738, ¶¶ 517, 521–529); those remaining are put to the service of system needs rather than to the use of the underlier having record title to them (R. 738, 745, ¶¶ 525, 572). Separate repair shops have been closed, the system now utilizing one central shop (R. 756, ¶¶ 651–652), located on the lines of an underlier (R. 406a–408a).

During the 40-odd years of the system's control by the debtor, much if not all of the underliers' physical properties has been retired from use and has been replaced by the debtor. In a registration statement filed with the Securities and Exchange Commission in 1941, Philadelphia Company, after a brief inventory of the system's assets, stated (R. 466a):

> Very little, if any, of the above enumerated property, other than land and buildings, was in existence at the time the Pittsburgh Railways System was unified in 1901 through leases, operating agreements and stock ownership. Most of it represents replacements and betterments either in respect of property in existence at that time, or as is more frequently the case, in respect of replacements to or betterments of such property. An accurate determination of what corporation in the system now has title to particular units of property, such as cars, tracks and overhead structures, would, in many instances, be most difficult and might involve recourse to the courts, and no attempt is made herein to allocate such property to the several corporations which comprise the system.

The treatment of the Guaranteed Underliers' properties in the unified operation was identical with that accorded the assets of the other underliers. The commingling, abandonment, disposal,

alteration and replacement of system property have applied equally to the Guaranteed Underliers.[6]

Thus, none of these companies has kept any records of its properties since 1902 (R. 795–796, 800, 803, ¶¶ 836, 838, 859, 872–873). Two officers of Suburban expressly admitted that they could not at present identify its properties (R. 523a–527a, 535a–537a). An officer of Monongahela, Pittsburgh & Birmingham and the latter's subsidiaries made a similar admission as to properties other than real estate, franchises and rights of way (R. 505a–508a). The president of Pittsburgh Incline Plane Co., another Guaranteed Underlier, was not sure of what its properties consisted, or when they were electrified, or whether its lease gave it an absolute right to the electrical equipment installed since the date of the lease (R. 535a–536a). The officers of these companies be-

[6] Alteration of routes, R. 762–763, 795, 799, ¶¶ 692 (3), 834, 852.

Abandonment of track, R. 762, 795, ¶¶ 692 (2), 834.

Disposal of real estate, R. 795, 798, ¶¶ 834, 849.

Sale of power plants, R. 727, 800, ¶¶ 512, 858.

Dismantling and disposal of car barns, R. 728–729, ¶ 513.

Replacement of original track and overhead, R. 508a–510a; R. 798, ¶ 848.

Relocation of original poles and feeder wires, R. 510a–511a; R. 798, ¶ 848.

Abandonment of bridges, R. 798, ¶ 848.

Scrapping of original rolling stock, R. 795, 796, 798, 799, ¶¶ 834, 838, 848, 851, 856.

See generally, R. 733–737, ¶ 517.

lieve a continuation of unified operation desirable, have not contemplated withdrawal of their properties from the system, and have no plans to resume separate operation (R. 383a–400a; R. 796–797, 801–802, 803, ¶¶ 841, 863–864, 876). The Special Master found that separate operation of the Guaranteed Underliers was "not a very practicable proposition" (R. 803, ¶ 880). It is inconceivable in any case that they could undertake independent public service.

Since 1902 these companies' only business has been the receipt of rentals and other income under their leases and the disbursement of bond interest and dividends (R. 185a, 187a, 191a; R. 795, 798, ¶¶ 833, 847). Irrespective of the insolvency of the debtor's street railway system as a whole, they are concerned only with the revenues they derive from the "beautiful guarantee of the Philadelphia Company" (R. 393a, 397a, 797, 802, ¶¶ 842, 864–865). They have acquiesced in the amalgamation of their properties into a single system from which they cannot withdraw.

The unitary character of the system is further indicated by various factors concerning the debtor and the Philadelphia Underliers evidencing the disregard of their separate corporate entities. Among other points may be noted a thorough interlocking of the officers and directors of the debtor and these underliers with their common parent, Philadelphia Company (R. 698–700, ¶¶ 382–390); various adjustments of operating

deficits through intercorporate loans, security transfers and other devices (R. 704–706, 720–724, ¶¶ 405–416, 474–482); the payment of dividends to Philadelphia Company simultaneously with the taking of loans from it (R. 702, 720, ¶¶ 395, 474–475); and the lack of books or the maintenance of only skeleton books by various underliers (R. 678, ¶ 283; cf. R. 301a). While numerous leases contained provisions specifying whether or not a lessor underlier was chargeable by its lessee for capital expenditures on the lessor's lines (R. 690–695, ¶¶ 344–355), the provisions were in practice not observed (R. 690, 810, ¶¶ 344, 1011), resulting at present in the virtual unascertainability of sums owing the underliers or the debtor on account of such expenditures (R. 575–576; cf. R. 689, 697–698, ¶¶ 339, 366). Accounting for capital expenditures subsequent to 1924 was admitted by Philadelphia Company's expert accounting witness to be "largely a matter of convenience in bookkeeping" (R. 332a). There were other accounting practices which were inconsistent with the status of the debtor and the Philadelphia Underliers as independent entities (R. 698, ¶¶ 367–370).

The system in reorganization—The guarantee problem

Almost since its inception the enterprise has had repeated and mounting deficits because of its crushing burden of fixed charges (R. 701,

¶ 391). Neither minor palliatives nor efforts at major adjustments, including an equity receivership in 1918–24 (which, however, failed to modify the debtor's obligations appreciably, R. 718–719, ¶¶ 470–471), proved availing. On May 10, 1938, at the instance of Philadelphia Company (R. 724, ¶ 483), the debtor filed a voluntary petition for reorganization in which it stated:

> A financial reorganization of the Debtor is imperative to the end that its street railway system may be continued as a unified system of transportation and the Debtor may continue to render adequate public service. [Not in printed record.]

Since that time the entire system has been in the custody of the court, the trustees continuing the system's operation on its unified basis (R. 58a; R. 675, ¶¶ 256–262). They have since neither affirmed nor disaffirmed the debtor's leases and operating agreements and have made no payments to the underliers for use and occupancy or on the debtor's lease or contract liabilities.

The two types of the debtor's obligations should be distinguished—interest requirements on the debtor's own outstanding securities, and fixed charges imposed upon the debtor by its undertakings pursuant to the leases and operating agreements running to it. As of May 10, 1938 the annual requirements on the debtor's out-

standing securities (other than car trust bonds) were as follows:[6a]

Bonds and collateral notes	$424,032
Interest on demand notes, approximately	500,000
Total, approximately	924,032

As of the same date the annual fixed charges of the debtor pursuant to its leases and operating agreements (other than on securities intercompany owned) were nearly three times this amount, as follows:

Rentals to underliers	$829,775
Interest on underliers' bonds	1,516,645
Interest on underliers' demand notes, approximately	100,000
Total, approximately	2,446,420

Of this sum of $2,446,420, the amount of $898,920[7] is an annual charge payable by the debtor to the Guaranteed Underliers (R. 585–588, Com-

[6a] The figures in this and the following table have been compiled from R. 585–588.

[7] The court below put the sum so owing at "half a million dollars a year plus taxes" (R. 951). It presumably arrived at this figure from R. 619, ¶ 32, which states that "In 1941, the net amount paid out by Philadelphia Company under the guaranteed leases was $467,413.52", exclusive of taxes. This, however, was a net figure, and did not include payments of rentals available for dividends on stocks of the Guaranteed Underliers or interest on their bonds held by Philadelphia Company itself, (*ib.* cf. R. 721–722, ¶ 480). On such stocks and bonds it would be unnecessary for Philadelphia Company as guarantor to make a circuitous payment to itself, but the debtor was nevertheless obligated on them under operating agreements to which it was a party.

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panies Nos. 29–36, 42, 45), in addition to those companies' taxes.[8]

The existence of the guaranteed leases is assigned as a principal reason for the impasse in the reorganization which has been pending for eight years.

Asked in hearings before the Special Master why Philadelphia Company, after bringing the system into the custody of the court, objected to the inclusion of the underliers in the reorganization, its senior vice-president and general counsel (R. 156a) gave two reasons. First, he stated, the company was charged with wrongdoing in the petition of the City of Pittsburgh initiating the present proceeding, and it felt obliged to resist (R. 727, ¶ 510).[9] Secondly, he gave it as his legal opinion that if the leases guaranteed by Philadelphia Company were to be terminated or destroyed by operation of law, without the participation or acquiescence of Philadelphia Company, the guaranteed lessors would be limited to the

[8] While under *Philadelphia Company* v. *Dipple*, 312 U. S. 168, the trustees have not paid the taxes owed by the underliers, the liability of the debtor for such taxes, including those owed by the Guaranteed Underliers, cannot be disputed. Cf. *Monongahela Street Ry. Co.* v. *Philadelphia Company, et al.*, 350 Pa. 603, 39 A. 2d 909, which held Philadelphia Company liable as guarantor for taxes owed by a Guaranteed Underlier. See R. 796, 800–801, ¶¶ 840, 861, 862.

[9] It should be noted, however, that Philadelphia Company opposed the inclusion of the underliers even prior to the City's petition (R. 724–726, ¶¶ 484–490).

assertion of a claim for damages not exceeding three years' rent (apparently under Section 202 of Chapter X, 11 U. S. C. § 602), and the liability of Philadelphia Company as guarantor would be limited correspondingly. This limitation, he feared, would not be available if Philadelphia Company could be successfully charged with having aided or acquiesced in the termination of the leases (R. 726, ¶ 491), which would presumably be possible if jurisdiction were held to encompass the underliers. In preference to its aiding a systemwide plan, therefore, Philadelphia Company, continuing the payments on its guarantees, has refused to place its underliers in reorganization voluntarily,[10] except on obviously impossible conditions (R. 724–726, ¶¶ 487–490), and has opposed systemwide jurisdiction. Its guarantee obligations have thus forced it to insist upon a position not only contrary to its understanding of reorganization practicalities but contrary to what it considers its own self-interest. Presumably, the reason for its objections to systemwide jurisdiction would be removed if such jurisdiction is imposed despite its best efforts to the contrary.

The Guaranteed Underliers, for their part, are presumably unwilling to litigate the extent of Philadelphia Company's liability on the guaran-

[10] The underliers' matured and unpaid bond issues are largely held 100% by Philadelphia Company or by the debtor (R. 539a; R. 629–631, ¶ 54; R. 721–724, ¶¶ 480–482).

tees any earlier than is essential. While the Philadelphia and Unguaranteed Underliers with debt securities outstanding have been found insolvent (R. 631, ¶¶ 55–56), and while, as to the Guaranteed Underliers, there is reason to believe that, were they dependent for their income solely upon their contribution to system earnings, they would also be insolvent, their solvency has been maintained by reason of Philadelphia Company's payments on its guarantees, and the Special Master found no insolvency as to them (R. 631, ¶ 57). They have denied the jurisdiction of the reorganization court over them.

With the reorganization thus deadlocked and in the unique situation presented by the foregoing combination of facts, the assertion of jurisdiction over the whole economic entity was the sole possible method for solving its interrelated financial problems.

ARGUMENT

The question presented arises out of the decision below that a reorganization court has the power, for plan purposes, to encompass corporations whose properties and economy are so inextricably commingled with those of the debtor in a single public utility operating unit, as to make their inclusion essential if the reorganization process is to be effective. While the fundamental question regarding the scope and flexibil-

ity of the Chapter X process in dealing with complex and relatively unique economic enterprises is important in the administration of the Bankruptcy Act, the precise issue here is not likely to be recurring, and since the holding below was clearly correct and no conflict of decisions is involved, it is our position that there is no occasion for further review.

1. A limitation of jurisdiction to the debtor alone would be useless as a means of achieving a reorganization. The debtor's fixed charges consist in only a minor degree of obligations on its own outstanding securities. The bulk of them, as we have shown, consist of rentals to underliers and liabilities on underliers' securities. These were assumed by the debtor pursuant to only seven leases and operating agreements running directly to it (R. 653–654, ¶¶ 161–163); other leases and agreements binding the debtor's system together run to various underliers, primarily United and Consolidated (R. 650–651). The reorganization process as applied to the debtor alone provides the means for the debtor's rejecting its seven undertakings, Bankruptcy Act, § 202, 11 U. S. C. § 602, but it provides no mandatory means for effecting their modification. So long as the court limits its authority to the debtor alone, modification of these contracts can be achieved only by the voluntary negotiation by the debtor and its seven contracting underliers of

new agreements on lower terms. The negotiations between the debtor and these mediate underliers, however, would require that such underliers, in turn, have some means of modifying their obligations to further lessor underliers and security holders. Efforts at voluntary negotiations would inevitably meet the resistance of hold-outs among security holders or lessor companies.[11] To bind dissenters, underlier companies in successive tiers would have to enter separate reorganization proceedings. Assuming this could be done without Philadelphia Company's assistance, which is doubtful, *supra,* n. 10, each such reorganization would be conducted with a wary eye watching the progress of all the others. Since the modification of each lease would be based upon a practical recognition of the inability of the debtor to meet existing rental charges, no single lessor could afford to accept a new lease at lower rental except in consideration of the simultaneous reduction of rentals on each of the other leases. For if the acknowledged objective of all the proceedings would be the continuation of the unified system on the basis of reduced intercompany obligations, each underlier and each securityholder would resist being subject to what it or he regarded as a disproportionately large cut (*cf.* R. 34a–35a). However, "one of the prime purposes

[11] *Cf.* R. 37a–39a.

of the bankruptcy law has been to bring about a ratable distribution among creditors of a bankrupt's assets; to protect the creditors from one another." *Young* v. *The Higbee Company,* 324 U. S. 204, at 210. A reorganization court should not subject securityholders to so doubtful a remedy as voluntary negotiations thus conducted, whose results depend on bargaining skill rather than a genuine attempt to ascertain values, and which can only generate pressures towards a larger and larger over-all capitalization.

Any alternative procedure which contains as one of its elements the separation of an important underlier's properties from the system must contemplate its separate operation as a working possibility. Since no such possibility exists,[12] any such alternative is obviously unfeasible. The trustee's power to reject the debtor's leases and

[12] *Cf.* the opinion of the court below (R. 941–942):

"* * * During the argument some suggestion was made by certain of the appellees that separate operation of certain of the underlying systems was physically possible. We do not doubt that fact. A trolley company with a franchise entitling it to run its cars on two city blocks may physically travel up and down that route. But nobody would contend that this kind of arrangement gave the type of public transportation service that a modern community needs. So here, even though some of the underlying companies have franchises for routes of very considerable distance and could, in some instances, get patrons into the center of town under their own separate systems, it is not seriously claimed that this method of operation would adequately meet community requirements."

agreements is therefore purely theoretical. So is his power to submit to a vote of security holders a genuine choice between their acceptance of a lease on lower terms or withdrawal.[13] The underliers and their security holders are similarly limited by the meaninglessness, on the facts here, of their theoretical right to repossession, and by the undoubted power of the reorganization court to preserve the unity of the system in the public interest. Their ability to compel the trustee to choose between affirmance and disaffirmance is therefore highly dubious, and so is their right to declare a forfeiture, assuming that such right exists at all without approval of the appropriate regulatory agency or perhaps the court. *Smith* v. *Hoboken Railroad, Warehouse and S. S. Connecting Co.,* decided April 29, 1946, No. 384, Oct. Term, 1945. It is significant on these points that, notwithstanding the fact, noted above, that neither payments of rent nor of use and occupancy have been made to the underliers since the inception of the reorganization and that the several leases and operating agreements have

[13] Such a set of alternatives, successfully presented to the Terre Haute security holders after this Court's decision in *Group of Institutional Investors* v. *Chicago, Milwaukee, St. P. & P. R. Co.*, 318 U. S. 523, see order of Sept. 19, 1945, in *Matter of Chicago, Milwaukee, St. P. & P. R. Co.*, N. D. Ill., E. Div., No. 60463, unreported, on its face implies that withdrawal of a company's properties from the system is physically and economically practicable.

been neither affirmed nor disaffirmed, no effort has been made by anyone to declare a forfeiture, to demand use and occupancy payments, or to compel an election by the trustee.

Other alternatives are equally unpromising. Straight bankruptcy proceedings are probably barred by statute to the debtor and the other system companies, because of the public interest in maintaining intact an operating public utility.[14] Dismissal of the Chapter X proceedings would invite the institution of individual actions seeking judgment or mortgage foreclosure. The consequent threat of the system's dismemberment would warrant a receivership. But apart from the fact that receivership proceedings are subject to the very vices and deficiencies that reorganization in bankruptcy was designed to remedy,[15] the receivership court would inevitably be confronted with the necessity in the public interest of exercising unitary jurisdiction over the entire system. With all its practical disad-

[14] Bankruptcy Act, § 4a, 11 U. S. C. § 22 (a); *Columbia Ry., Gas & Electric Co.* v. *South Carolina*, 27 F. 2d 52 (C. C. A. 4), affirming *In re Columbia Ry., Gas & Electric Co.*, 24 F. 2d 828 (E. D. S. C.); but *cf. In re Grafton Gas & Electric Light Co.*, 253 Fed. 668 (N. D. W. Va.).

[15] H. Rep. No. 1409, 75th Cong., 1st Sess., p. 37 *et seq.*; *Duparquet Huot & Moneuse Co.* v. *Evans*, 297 U. S. 216, 218–219; *Securities and Exchange Commission* v. *United States Realty & Improvement Co.*, 310 U. S. 434, 448–450.

vantages, this procedure would still leave the court with the same legal problem which confronts it in this case; namely, whether it possessed the power to effectuate a reorganization plan for the entire system.

The court below, unwilling to permit the debtor and the underliers to remain indefinitely *in custodia legis* (R. 942–943), adopted the only available course in holding that jurisdiction for plan purposes extended to the constituent system companies. Any other result would have been an intolerable impairment of the functions of a reorganization court.

2. This ruling, required by a unique fact situation, was admittedly without direct precedent. There were, however, "signposts to mark the way," as the circuit court of appeals put it (R. 950), and its decision was along judicially accepted lines.

The traction properties of the underliers have all been in the possession of the reorganization court since the inception of the proceeding and in that of the debtor prior thereto. Such possession alone is sufficient to confer jurisdiction. *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 737–738. While with respect to property to which title is claimed adversely or as to which a lien is asserted, the court may confine the exercise of its powers to passing on the question of title or the

validity of the lien, the "malleable processes of courts in bankruptcy give assurance of a remedy than can be moulded and adapted to the needs of the occasion", *Steelman* v. *All Continent Company,* 301 U. S. 278, 290, and clearly permit jurisdiction to the extent defined by the court below.[16] The properties allegedly belonging to the debtor and individual underliers are, as we have shown, inextricably commingled. The value of any underlier's interest obviously depends on the utilization of its assets as part of the unitary system. In addition, there is a paramount public interest in retaining the system as a unit. Under such circumstances the court below was clearly correct in deciding that the interests of the various underliers and their security holders could be determined only by means of a systemwide reorganization plan, and that jurisdiction to this end existed.

A common administration of an insolvent parent and its subsidiaries where required by the facts has been held within the powers of a court in

[16] See, on the flexibility of the reorganization process, Byrne, *The Foreclosure of Railroad Mortgages in the United States Courts*, in *Some Legal Phases of Corporate Financing, Reorganization and Regulation*, 1917, p. 77; Cutcheon, *An Examination of Devices Employed to Obviate the Embarrassments to Reorganizations Created by the Boyd Case*, in 8 Lectures on Legal Topics, 1931, p. 35; Swaine, *Reorganization of Corporations: Certain Developments of the Last Decade*, id. at p. 133.

equity receivership (*Trustees System Co. of Penna.* v. *Payne,* 65 F. 2d 103 (C. C. A. 3); *Commerce Trust Co.* v. *Woodbury,* 77 F. 2d 478 (C. C. A. 8)), and in bankruptcy (*Central Republic Bank & Trust Co.* v. *Caldwell,* 58 F. 2d 721 (C. C. A. 8); *Stone* v. *Eacho,* 127 F. 2d 284, (C. C. A. 4), certiorari denied, 317 U. S. 635).[17] These cases were based on the often utilized principle that separate corporate entities will be ignored where their recognition would defeat the remedial purpose of a statute. E. g., *Anderson* v. *Abbott,* 321 U. S. 349, *Higgins* v. *Smith,* 308 U. S. 473, 477–8. On this ground jurisdiction was extended in the *Trustees System Co., Commerce Trust Co.* and *Central Republic Bank* cases, *supra,* to subsidiaries not alleged or found insolvent. The subjection of the Guaranteed Underliers here to the reorganization powers of the court is thus in accord with equity receivership and bankruptcy precedents.

Furthermore, insofar as system earnings are concerned, all the underliers appear to be insolvent. None of them is capable of functioning independently and of meeting obligations to both security holders and the public. And

[17] Language in *Price* v. *Gurney,* 324 U. S. 100, 107, indicating the necessity for the filing of a petition by a person authorized to do so by the terms of the Bankruptcy Act was not addressed to the situation where the disregard of separate corporate entities was involved, or where unlike that case (324 U. S. at 105) other remedies were unavailable.

a "unitary economic foundation" for the enterprise (R. 951) is, as the court below pointed out, impossible if the rental, interest and tax obligations of the Guaranteed Underliers alone are to be borne undiminished by the operations of the system. Whatever the effect of Philadelphia Company's guarantees, a fair and equitable equivalent, based upon the contribution of their assets to the earnings of the system, is all that the Guaranteed Underliers and their security holders can claim as against the debtor. *Reconstruction Finance Corp.* v. *Denver & R. G. W. R. Co.,* decided June 10, 1946, Nos. 278–282, Oct. Term, 1945, slip sheet opinion, pp. 26–27; *Wright* v. *Union Central Life Ins. Co.,* 311 U. S. 273, at 278.

The disregard of a corporate entity normally permits a court to look directly to the entity's stockholders or to an affiliate through stock ownership. Here the operational unity embraced the assets of the Guaranteed Underliers as inextricably as those of the Debtor and the other underliers. The Guaranteed Underliers knowingly contributed their properties to it and in the public interest it must be preserved unbroken. *Cf. Reconstruction Finance Corp.* v. *Denver & R. G. W. R. Co., supra,* slip sheet opinion at p. 29. Thus, notwithstanding the fact that the stockholdings linking the Guaranteed Underliers to the debtor were not as extensive as those linking the Philadelphia Underliers (R. 618, ¶ 26), there was an

adequate factual basis for the step taken by the court below.[18]

3. Because of the parties' contentions the opinion below discussed the question of a possible impingement of bankruptcy powers upon state law. But its holding that state law did not forbid or limit its jurisdiction in reorganization did not involve, either as a premise or a conclusion, the determination of any question contrary to state law.

None of petitioners contends that a systemwide reorganization, of itself, is contrary to Pennsylvania law in the sense that a state insolvency or equity receivership proceeding for a debtor under present circumstances has been held by a Pennsylvania court not to comprehend an aggregation of underliers comprising a unitary system. Nor was local law violated by any other ruling of the lower court. The circuit court of appeals did not hold that the underliers were not valid corporations. It did not hold that the leasing arrangements authorized by state law were invalid. It did not

[18] This question was not involved in *New York Trust Co.* v. *N. Y. & Greenwood Lake Ry. Co.*, No. 8943, 3d circuit, July 17, 1946, amended July 23, 1946, for there the appellee company, which, partially on the authority of the decision here sought to be reviewed, was subjected to the jurisdiction of the court in which Erie Railroad was in reorganization, was 95% stock owned by the Erie. The issue there was the power of a court other than the reorganization court to fix the fees of an indenture trustee and its counsel for services rendered the appellee.

hold that the leases were conveyances or had any legal effect other than that of leases.[19] It did not hold that, in determining the substantive rights of security holders to receive their equitable equivalents under a systemwide plan, the property which under state law is an underlier's should under the plan be treated as belonging to another underlier or as the debtor's. The prayer which it ordered granted, as pointed out by the Special Master, "asks for no surrender of anything in the possession of the underliers, and asks for no conveyance from or coercion of the underliers" (R. 815, ¶ 1052). The court merely held that with the debtor's system an integral unit, the formal intercorporate arrangements, while permitted under state law, could not thwart the indispensable exercise of bankruptcy jurisdiction (R. 948).

Petitioners contend, however, that state law was violated in that Chapter X of the Bankruptcy Act limits jurisdiction of the reorganization court

[19] We may add that, despite the absence of such a ruling by the court, we have serious question whether on the facts here, where effective repossession by lessor underliers is impossible and has not been attempted, the leases are anything other than security devices giving rise to contractual rights to repayment. Such rights are replaceable in reorganization by new evidences of interest, whose total will be commensurate with the earning power of the system and which will be distributed so as to give a fair and equitable equivalent of the rights they supplant. But the issue is not raised until the lessors' interests are so treated under a plan.

to the property of the debtor. Asserting that under state law the leases reserved property in the system assets to the underlier corporations, they argue that such property is beyond the jurisdiction of the court. The contention appears to be based on a misapprehension of the provisions relied on in its support.

Section 111 of Chapter X, 11 U. S. C. § 511, which confers upon the court "exclusive jurisdiction of the debtor and its property, wherever located" was not intended to confine the powers of the reorganization court to property to which a debtor had title. In straight bankruptcy, the court, upon adjudication, secures jurisdiction over all property in the possession of the bankrupt whether or not he has title. *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, at 737. This was true also in equity receivership as to property in a debtor's possession within the territorial jurisdiction of the court. 2 Gerdes on *Corporate Reorganizations* (1936), pp. 1360–1365. The effect of the quoted language of Section 111, which also appears in Sections 77(a) and 77B(a), 11 U. S. C. § 205(a) and former § 207(a), was to extend the reorganization court's exclusive jurisdiction to property in the debtor's possession whether or not within the territorial jurisdiction of the court. Cf. *Continental Illinois Nat'l Bank & Trust Co.* v. *Chicago, R. I. & P. Ry. Co.*, 294 U. S. 648. The language was not designed to deny to a re-

organization court jurisdictional powers, already vested in courts of straight bankruptcy or receivership, over assets in the possession of a debtor although admittedly not his property. On the contrary, under Sections 114 and 115 of Chapter X, 11 U. S. C. §§ 514, 515, such powers are expressly conferred upon the court in reorganization proceedings. See also Bankruptcy Act, Sections 2a, 2a (6), 11 U. S. C. §§ 11a, 11a (6). In the exercise of such powers the court may deal in a binding way with the reversionary interest of a lessor to a debtor. *Warren* v. *Palmer,* 310 U. S. 132, at 138.

Nor was Section 216 (2), 11 U. S. C. § 616 (2), permitting a plan to "deal with all or any part of the property of the debtor," designed to have a limiting effect. It was derived from Section 77B(b)(10), formerly 11 U. S. C. § 207(b)(10), see S. Rep. 1916, 75th Cong., 3d Sess., p. 34, and was intended, in the interests of flexibility, to permit a plan to deal with less than the entire estate. 2 Gerdes on *Corporate Reorganizations* (1936), p. 1760. Neither this provision, however, nor Section 111, *supra,* limits jurisdiction solely to assets over which the debtor has legal title under state law.[20]

[20] No acquiescence is intended by this argument in petitioners' contention that, on the facts here, the underliers have present legal title under state law to specific indentifiable assets in the system. See *supra*, p. 10.

Conceivably the differentiation of properties belonging respectively to the debtor and the individual underliers, insofar as is possible in their present commingled state, may become necessary or useful in determining such problems as the effect of after-acquired property clauses, the validity of liens or the value of collateral assets for purposes of distribution under a plan. The determination of these and similar issues by plan approval and confirmation may give rise to such reviewable questions as whether or not "appropriate regard" was shown "for rights acquired under state law," *Heiser* v. *Woodruff*, decided April 22, 1946, No. 496, Oct. Term, 1945, *cf. American Surety Co.* v. *Sampsell*, decided February 25, 1946, No. 142, Oct. Term, 1945. No such substantive determinations have been made by the circuit court of appeals, however, and no conflict with state law appears in its ruling.

4. Nor did the court below, in reaching its conclusion, depart from the decision of this Court in *Philadelphia Company* v. *Dipple*, 312 U. S. 168. That case held that taxes of the underliers could not be paid as expenses of administration of the estate. As the court below pointed out (R. 947), the case did not involve the public interest in maintaining the unified system. Nor did it concern the question of finding the method for terminating the protracted reorganization (R. 942). It was not inconsistent to recognize the formal

legal entities comprising the system as separate for tax purposes and to insist upon their unity for the different problems of plan jurisdiction. *Irving Trust Co.* v. *Kaminsky,* 22 F. Supp. 362 (S. D. N. Y.), citing *Corsicana National Bank* v. *Johnson,* 251 U. S. 68, 88, 89. Note, *Insolvency as a Requisite to Piercing the Corporate Veil,* 82 U. Pa. L. R. 868 (1934).

Furthermore, the Court in the *Dipple* case was concerned over the possibility of preferences in favor of certain underliers if taxes which it was sought to have the trustees pay on their behalf should exceed sums properly due them for use and occupation or for rent, for it recognized the great difficulty in apportioning system receipts among underliers in ratio to their contribution to the enterprise. 312 U. S. at 174. Some effort to ascertain the individual underliers' contribution to the enterprise must presumably be made before system earnings can be fairly distributed to them and in turn to their security holders, and the proposed systemwide plan in fact represents an attempt at such a determination (R. 573–575). The various theoretical alternatives outlined above (pp. 19 *ff.*) fail to achieve this result, while one such method—negotiation for reduced intercorporate obligations and the binding of dissenters by the entry into reorganization of successive tiers of underliers—is, apart from obvious difficulties, rife with the possibility

of preferences. Jurisdiction for a systemwide plan, rather than contravening *Philadelphia Company* v. *Dipple*, actually carries out its intent.

CONCLUSION

The petitions for writs of certiorari should be denied.

Respectfully submitted.

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